

REVISED AGENDA – January 4, 2000, Business Taxes Committee Meeting
Proposed Amendments to Clarify Application of Tax to Sales or Leases of On-Premise Electric Signs
Regulation 1521, *Construction Contractors*
Regulation 1660, *Leases of Tangible Personal Property – In General*

<p>Action 1 – Consent Item – Application of tax to “on-premise” electric signs furnished and installed by a construction contractor.</p> <p>Amend Regulation 1521, <i>Construction Contractors</i>, by the addition of subdivision (c)(12), <i>On-Premise Electric Signs</i>.</p>	<p>Adopt proposed amendment as agreed upon by industry and staff.</p>
<p>Action 2 – Application of Tax to Leases of On-Premise Electric Signs.</p> <p>Amend subdivision (d)(6), <i>Neon Signs</i>, of Regulation 1660, <i>Leases of Tangible Personal Property – In General</i>.</p>	<p>Adopt either:</p> <ol style="list-style-type: none"> 1) Staff’s recommendation to make no amendments to Regulation 1660, or 2) Industry’s proposal to amend subdivision 1660(d)(6) to apply to on-premise electric signs in general and exclude from taxable lease receipts charges for payment or reimbursement of personal property taxes and for maintenance and insurance charges.
<p>Action 3 – Authorization to Publish – Amendment to Regulation 1521</p>	<p>Direct the publication of the proposed amendments to Regulations 1521 as adopted in the above actions.</p> <p>Operative Date: October 1, 2000. Implementation: Upon OAL approval.</p>
<p>Action 4 – Authorization to Publish – Amendment to Regulation 1660</p>	<p>Direct the publication of the proposed amendments to Regulations 1660 as adopted in the above actions.</p> <p>Operative Date: October 1, 2000. Implementation: Upon OAL approval.</p>

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Regulation 1521, *Construction Contractors*
Regulation 1660, *Leases of Tangible Personal Property – In General*

ACTION 1 – Consent Item

Action Item	Staff and Industry's Proposed Regulatory Language
<p>Action 1 – Consent Item – Application of tax to “on-premise” electric signs furnished and installed by a construction contractor.</p> <p>Exhibit 2, Page 1</p>	<p>Regulation 1521(c), Particular Applications</p> <p><u>(12) On-Premise Electric Signs</u></p> <p><u>(A) An on-premise electric sign is any electrically powered or illuminated structure, housing, sign, device, figure, statuary, painting, display, message, placard, or other contrivance or any part thereof affixed to real property and intended or used to advertise, or to provide data or information in the nature of advertising, for any of the following purposes: 1) To designate, identify, or indicate the name or business of the owner or occupant of the premises upon which the advertising display is located, and 2) To advertise the business conducted, services available or rendered, or the goods produced, sold, or available for sale, upon the property where the advertising display has been erected.</u></p> <p><u>(B) Application of tax. An on-premise electric sign is a fixture. Notwithstanding the provisions of 1521(b)(2)(B), operative October 1, 2000, tax applies to 33 percent of the sales price of on-premise electric signs that are furnished and installed by the seller. “Sales price” includes charges for materials, fabrication labor, installation labor, overhead, profit, and other charges associated with the sale and installation of the sign. If a contract provides that a contractor is to install an on-premise electric sign furnished by a third party, the charges for installation are not taxable. If a seller furnishes but does not install an on-premise electric sign, the seller is a retailer of the sign and tax applies to the total selling price.</u></p> <p><u>Separately stated charges for transportation are subject to tax as defined in Regulation 1628, <i>Transportation Charges</i>.</u></p>

REVISED AGENDA – January 4, 2000, Business Taxes Committee Meeting
Proposed Amendments to Clarify Application of Tax to Sales or Leases of On-Premise Electric Signs
Regulation 1521, *Construction Contractors*
Regulation 1660, *Leases of Tangible Personal Property – In General*

Action Item	Current Regulatory Language (Recommended by Staff)	Industry's Proposed Language
<p>Action 2, Application of Tax to Leases of On-Premise Electric Signs</p> <p>Exhibit 2, Page 2</p>	<p>Regulation 1660:</p> <p>(d) Particular Applications.</p> <p>(6) Neon Signs. A lease of a neon sign that is personal property is subject to the provisions of the Sales and Use Tax Law as any other lease of personal property.</p>	<p>Regulation 1660:</p> <p>(d) Particular Applications.</p> <p>(6) Neon-On-Premise Electric Signs. <u>An on-premise electric sign is any electrically powered or illuminated structure, housing, sign, device, figure, statuary, painting, display, message, placard, or other contrivance or any part thereof affixed to real property and intended or used to advertise, or to provide data or information in the nature of advertising, for any of the following purposes: 1) To designate, identify, or indicate the name or business of the owner or occupant of the premises upon which the advertising display is located, and 2) To advertise the business conducted, services available or rendered, or the goods produced, sold, or available for sale, upon the property where the advertising display has been erected. On-premise electric signs are tangible personal property.</u></p> <p>A lease of an neon-on-premise electric sign that is personal property, <u>including neon signs</u>, is subject to the provisions of the Sales and Use Tax Law as any other lease of personal property <u>except, operative October 1, 2000, the measure of tax does not include amounts paid for personal property taxes on the leased property or amounts paid to the lessor for insuring or maintaining the leased property.</u></p>

REVISED AGENDA – January 4, 2000, Business Taxes Committee Meeting
Proposed Amendments to Clarify Application of Tax to Sales or Leases of On-Premise Electric Signs
Regulation 1521, *Construction Contractors*
Regulation 1660, *Leases of Tangible Personal Property – In General*

ACTION 3, Authorization to Publish - Amendment to Regulation 1521	Direct the publication of amendment to Regulation 1521 as adopted by the above actions. Operative Date: October 1, 2000. Implementation: Upon OAL approval.
ACTION 3, Authorization to Publish - Amendment to Regulation 1660	Direct the publication of amendment to Regulation 1660 as adopted by the above actions. Operative Date: October 1, 2000. Implementation: Upon OAL approval.

Issue Paper Number 99-063



- ☐ Board Meeting
- ☒ Business Taxes Committee
- ☐ Customer Services Committee
- ☐ Legislative Committee
- ☐ Property Tax Committee
- ☐ Technology & Administration Committee
- ☐ Other

APPLICATION OF TAX TO SALES AND LEASES OF ELECTRIC SIGNS:

REGULATION 1521, *CONSTRUCTION CONTRACTORS*

REGULATION 1660, *LEASES OF TANGIBLE PERSONAL PROPERTY – IN GENERAL*

I. Issue

Should Regulations 1521, *Construction Contractors*, and Regulation 1660, *Leases of Tangible Personal Property – In General*, be amended to clarify the application of tax to sales and leases of electric signs?

II. Staff Recommendation

Staff recommends: 1) Regulation 1521 be amended to tax the sale of an on-premise electric sign furnished and installed by the seller on 33% of the total selling price, and 2) No change to the current provisions of Regulation 1660, which require that property tax reimbursements and mandatory charges for maintenance and insurance be included as part of taxable lease receipts.

III. Other Alternatives Considered

Alternative 1

Industry agrees with staff's proposed amendment to Regulation 1521. However, industry proposes that Regulation 1660 be amended to exclude property tax reimbursements and charges for maintenance and insurance from taxable lease receipts.

Issue Paper Number: **99-063**

IV. Background

Discussion – Application of Tax to Sales of Electric Signs

In his letter of September 23, 1999, Mr. Robert M. Aran, General Counsel for the California Electric Sign Association (hereinafter referred to as industry), detailed several concerns with the current application of the sales and use tax to sales and leases of on-premise electric signs. Industry's letter was a followup to a meeting held with staff in March 1999 and letters from the staff to industry dated May 7, 1999 and August 6, 1999. Staff's letters detailed the application of tax to sales and leases of signs under current law. The application of tax to sales of signs will be discussed in this section. The application of tax to leases of signs will be discussed in the following section.

Industry and staff met on October 4 and November 10, 1999 to discuss this issue. Industry is concerned about the application of tax to sales of signs because of the difficulties of determining which labor charges are taxable when a sign is furnished and installed by a sign company. Electric signs can be custom fabricated by the seller and installed on real property, or purchased as partially completed with fabrication being completed as part of the installation on real property. Under the sales and use tax law, the fabrication labor is taxable and the installation labor is exempt. However, allocating charges between fabrication and installation labor is often difficult because, on many jobs, the distinction between fabrication and installation is unclear. Industry feels that trying to apply this distinction to the sales and installation of on-premise electric signs is unrealistic and unwarranted and creates inequities in the industry. Industry also stated that this distinction creates audit problems. Audits of member companies sometimes result in large liabilities because the companies do not understand how to properly allocate and document exempt labor charges. It requests a simpler method for reporting tax that would create and maintain a level playing field for all members of the industry: those companies that both manufacture and install signs and those companies that only install signs.

Application of Tax to Sales of Signs Under Regulation 1521

The application of tax to signs in general is covered in Regulation 1521, *Construction Contractors*. This regulation defines a construction contract as a contract entered into to erect, construct, alter or repair real property including, but not limited to, buildings or other structures, fixed works such as waterways, generating plants, electrical transmission or communication lines, or public works such as highways, airports, sewers and waterworks. Contracts for paving, central heating and air, and electrical jobs are specifically defined as construction contracts.

The regulation makes a distinction between types of property furnished under a construction contract: materials, fixtures, and machinery and equipment. "Materials" include construction materials and components or other tangible personal property which, when attached to the real property, lose their identities to become an integral and inseparable part of the real property. Construction contractors are considered consumers of materials, and tax applies to the sale of the materials to the contractor or to the use of the materials by the contractor. "Fixtures" include items that are accessories to real property and do not lose their identities as accessories when installed. Construction contractors are considered retailers of fixtures unless they furnish the fixtures to the United States government. Because construction contractors are retailers, tax applies to the contractor's separately stated selling price. If no selling price is stated, tax is due on the cost of the fixture to the contractor. For fixtures acquired in a

Issue Paper Number: **99-063**

completed condition, “cost” is deemed to be the purchase price. For a self-manufactured fixture, “cost” is:

- The price at which a similar fixture is sold ready for installation, or
- If there are no similar fixtures, “cost” is the price stated in the records of the contractor, or
- If cost cannot be established from the records, it is the total of material cost, direct labor, specific factory costs, excise tax, a pro-rata share of overhead and a reasonable profit.

Contractors are consumers of fixtures furnished to the United States government.

“Machinery and equipment” is defined as property intended to be used in manufacturing, processing, or services not essential to the real property. Construction contractors are retailers of machinery and equipment.

Ruling No. 11, published in 1939, established the categorization of property furnished under construction contracts as materials or fixtures. The category for machinery and equipment was established by Ruling No. 12 in 1941 for contractors making sales to the United States government. When Rulings No. 11 and 12 were revised to create Regulation 1521, all three categories were included in the regulation. Ruling No. 11 classified signs as fixtures. This classification was continued in Regulation 1521. If a sign is considered a fixture, tax applies to the contractor’s separately stated selling price for the sign, or, if not separately stated, to the contractor’s cost of the sign.

Although the regulation generally defines signs as fixtures, certain types of signs do not qualify, for example, signs that are built into and become an integral part of the real property. Such a sign is considered a use of materials to improve the realty to which it is attached. The contractor furnishing this type of sign is a consumer of the materials and is liable for tax on their cost.

It should also be noted that charges for installing a sign on realty are nontaxable. Sections 6011 and 6012 of the Revenue and Taxation (R&T) Code exclude installation charges from the definition of “sales price” and of “gross receipts from a sale.” On the sale of a sign qualifying as a fixture, installation labor includes charges for mounting the sign on real property, for example, a pole or a wall.

Industry Proposals

Industry initially proposed that sellers of on-premise electric signs be treated as consumers of materials. Staff agreed that this approach has the virtue of simplicity. However, staff explained to industry that being consumers would require companies to pay sales tax reimbursement or use tax on all materials at the time of purchase. Industry noted that this requirement would have a detrimental effect on the cash flow of member companies. Consequently, industry decided that being consumers was not a viable option. However, industry did urge staff to consider a reporting method that would simplify reporting for the industry and minimize audit problems. To achieve these goals, industry proposed that taxable measure be based on a percentage of total charges. Industry proposed a percentage that was equivalent to the cost of materials consumed on sales of on-premise electric signs. Based on a survey of member companies, industry suggested that 20 percent was the average equivalent of cost of materials on sales of on-premise electric signs.

Issue Paper Number: **99-063**

Staff agrees that using a standard percentage is a reasonable approach. On-premise electric sign companies comprise a limited, distinct group within the construction industry that can appropriately use such a method. Staff also believes that a carefully crafted method, such as percentage of total sales, provides simplicity for the on-premise electric sign industry without materially affecting state revenues. However, staff pointed out to industry that, under Regulation 1521, member companies are retailers of on-premise electric signs. Consequently, members of the industry were liable for tax not merely on the cost of materials used to self-manufacture signs, but also on fabrication labor, overhead costs, and profit. Consequently, staff felt that 20 percent was inadequate.

Industry and staff agreed that a further survey of industry members was needed to establish a reasonable percentage. Industry provided the names of eighteen companies and staff obtained sales information reported on sales and use tax returns filed by these companies during 1998. Staff included sixteen of the companies in its survey. Two of the companies could not be used because they reported either net taxable sales or no taxable sales. To determine an average percent of taxable measure in reported retail sales, staff adjusted out non-retail sales such as lease receipts, out-of-state sales, resales, and sales to the U.S. government. Of the remaining retail sales, the survey showed that 42 percent had been reported as taxable. A schedule and graph summarizing results are attached as Exhibit 3.

To determine the accuracy of the overall findings, staff reviewed recent audit results for 11 of the companies surveyed. The audits found that these companies were reporting sales of on-premise electric signs correctly. Audit items were generally unreported ex-tax purchases of supplies and equipment.

Subsequent to completing the survey, staff met with industry about the findings. Based on the findings, industry conceded that 20 percent was too low. However, industry also felt that 40 percent was too high. In its analysis of one of its largest member companies, industry found that this company had a taxable percentage that was materially lower than 40 percent. This company was included in the group of member companies surveyed by staff and staff's findings for this company concurred with industry's findings. To ensure that a standard percentage would not result in an excessive tax burden to member companies, staff and industry agreed that a lower percentage should be used. After some discussion, both industry and staff agreed to 33 percent as a reasonable compromise.

In the course of the discussions, industry noted that it was not interested in retroactive application of any amendments to Regulation 1521. Industry felt that it needed adequate time to inform member companies of the change and the member companies would need time to change accounting practices. Industry and staff agreed that the most practical operative date was October 1, 2000.

Discussion – Application of Tax to Leases of Signs

Industry Proposals

Industry questions the application of tax to specific charges included in lease contracts. It also proposes that on-premise electric signs be treated as something other than fixtures under the Sales and Use Tax Law. Questioned charges include reimbursement of real property tax paid by the lessor, and the mandatory charges for insurance and maintenance, which industry feels are required under the federal Internal Revenue Code. Industry proposes that these items be excluded from taxable lease receipts. Industry feels that including property tax reimbursements in taxable lease receipts constitutes a burdensome double taxation. Industry explained that the mandatory charges for insurance and

Issue Paper Number: **99-063**

maintenance are required under the Internal Revenue Code to demonstrate the risk of ownership of leased signs. Industry feels that compliance with federal requirements should not put the lessors at risk for increased sales or use tax. Industry also notes that mandatory charges for insurance and maintenance are merely a recapture of costs associated with protecting and maintaining the electric sign. These charges generate no profit for the lessor of the sign and there is no transfer of tangible personal property associated with the charges. Finally, industry feels that on-premise electric signs should not be treated as fixtures or personal property under the Sales and Use Tax Law. Industry notes that these signs are generally attached to real property and their character differs materially from fixtures or personal property.

During the discussions with staff, industry also voiced its concerns about having to report sales or use tax on the entire amount of real property tax assessed against a leased on-premise electric sign. Industry explained that a lessor of on-premise electric signs is often leasing not only the electric sign fixture, but also the supporting structure. Under Sales and Use Tax Law, the structure qualifies as nontaxable real property. Industry felt it was unreasonable to report tax on the portion of real property tax assessed against the structure. In response, staff noted that a lease, which includes both real and tangible personal property, is taxable only on the lease receipts for the tangible personal property. However, staff also noted that the lease contract must have a clear allocation between payments due on the real and tangible personal property. With such an allocation, separately stated charges for reimbursement of real property tax assessed against the structure would not be subject to sales or use tax. Because the contracts were not available for review, staff recommended and industry agreed to handle this matter through a letter inquiry to the Legal Department.

Application of Tax Under Section 6011 and Regulation 1660

The application of tax to charges for leased property is governed by Section 6011 of the R&T Code and Regulation 1660. Section 6011 states that “‘sales price’ means the total amount for which tangible personal property is sold or leased or rented.” The section specifically excludes from “sales price” charges for cash discounts, refunds on returned property, installation labor, certain excise taxes, and technology transfer agreements.

Regulation 1660 applies the provisions of Section 6011 to leases. Subdivision 1660(c)(1) states that a lease is a “sale” and a “purchase,” and tax is measured by the rentals payable. It further provides that “rentals” subject to tax “include any payments required by the lease including amounts paid for personal property taxes.” With respect to insurance and maintenance, Regulation 1660(c)(1)(F) provides that rentals subject to tax do not include amounts paid to the lessor for “separately stated optional insurance charges, maintenance or warranty contracts.” Consequently, separately stated charges for optional maintenance or insurance would not be subject to tax.

Regulation 1660 includes provisions governing the application of tax to property affixed to realty. Under subdivisions 1660(d)(7), tangible personal property “includes any leased fixture affixed to realty if the lessor has the right to remove the fixture upon breach or termination of the lease agreement, unless the lessor of the fixture is also the lessor of the realty to which the fixture is affixed.” Leases of structures together with the component parts of the structure are considered leases of real property. However, leased fixtures which are component parts but which are being leased by someone other than the lessor of the structure, are considered tangible personal property subject to sales or use tax. It should be noted that these provisions require the fixture to be tax-paid at source.

Issue Paper Number: **99-063**

Staff Response to the Industry Proposal

Staff believes that no change should be made to the application of tax to leases of on-premise electric signs. Under Section 6011 and Regulation 1660, charges not specifically excluded from sales price are includible in the measure of tax. It is irrelevant whether the source of the charges is reimbursement of property taxes or a billing method mandated by a federal code. Regulation 1660 has considered electric neon signs personal property since at least 1976 in subsection (d)(6) and has provided that tax applies to the total rental or lease receipts unless a specific exclusion is allowed for separately stated charges. Staff is of the opinion that a change to the taxable status of the property tax reimbursements and insurance and maintenance charges requires legislative action. It should also be noted that the issue of excluding property tax reimbursements from taxable lease receipts was considered at the November 1999 BTC meeting. At that meeting, the BTC decided that these charges are properly taxable.

Staff is also of the opinion no change should be made to the definition of leased signs as fixtures. Signs have been classified as fixtures since the inception of the sales tax. A sign that is leased does not lose its identity as an accessory to real property on which it is installed. However, as noted in the preceding section, subdivision 1660(d)(7) does treat fixtures as real property when the lessor owns and leases both the real property and the fixture. Staff recommends that lessors of on-premise electric signs request an opinion whether this provision applies to leased on-premise electric signs.

V. Staff Recommendation

A. Description of the Staff Recommendation

Staff recommends: 1) Regulation 1521 be amended to tax sales of on-premise electric signs furnished and installed by the seller on 33% of the total selling price, and 2) No change to the current provisions of Regulation 1660, which require that property tax reimbursements and mandatory charges for maintenance and insurance be included as part of taxable lease receipts.

B. Pros of the Staff Recommendation

Regulation 1521:

- Simplifies application of tax to sales of on-premise electric signs.
- Establishes the same basis of reporting for all members of the industry.
- Maintains consistency with statutory and regulatory authority.

Regulation 1660:

- Maintains consistency with the application of tax to other business expenses of a lessor that are passed to the lessee.
- Does not require legislative action.

Issue Paper Number: **99-063**

C. Cons of the Staff Recommendation

Regulation 1521:

- May increase tax liability for sellers currently below the calculated average.
- May cause some sign companies to change from being consumers to retailers.

Regulation 1660:

- Would continue to enable the issue of the inclusion of property tax and mandatory insurance and maintenance reimbursements in taxable rental receipts to be raised.

D. Statutory or Regulatory Change

No statutory change required. However, it does require an amendment to Regulation 1521.

E. Administrative Impact

None

F. Fiscal Impact

1. Cost Impact

Costs related to the amendment would be absorbable.

2. Revenue Impact

None. See Revenue Estimate.

G. Taxpayer/Customer Impact

Proposed amendment to Regulation 1521 will affect companies that fabricate and install on-premise electric signs. Staff will be required to notify these taxpayers of the change.

H. Critical Time Frames

Operative date is October 1, 2000.

VI. Alternative 1

A. Description of the Alternative

Issue Paper Number: **99-063**

Industry agrees with staff's proposed amendment to Regulation 1521. However, industry proposes that Regulation 1660 be amended to exclude property tax reimbursements and charges for maintenance and insurance from taxable lease receipts.

B. Pros of the Alternative

- Some lessees would experience tax savings measured by the property tax currently being charged on leases.
- Would reduce confusion for consumers who believe they are being charged a tax on a tax.

C. Cons of the Alternative

- No statutory basis
- Would potentially affect all lease transactions.
- Would result in a revenue loss to the state. (See Revenue Estimate.)

D. Statutory or Regulatory Change

Proposed amendments to Regulation 1660 require that statutory changes be made to R&T Code Sections 6011 and 6012.

E. Administrative Impact

Minimal administrative impact expected. On-site electric signs are leased by a limited number of companies. Notification would not significantly increase workload. Proposal is not retroactive.

F. Fiscal Impact

1. Cost Impact

Costs related to the proposed amendments would be absorbable.

2. Revenue Impact

Alternative would result in an estimated revenue loss of less than \$100,000. See Revenue Estimate.

G. Taxpayer/Customer Impact

Proposed amendment to Regulation 1660 might require lessors to reprogram billing software so that property tax reimbursements are separately stated as nontaxable charges. Lessees would have some tax relief.

Issue Paper Number: **99-063**

H. Critical Time Frames

Proposed operative date is October 1, 2000.

Prepared by: Program Planning Division, Sales and Use Tax Department

Current as of: December 22, 1999

BOARD OF EQUALIZATION
REVENUE ESTIMATE

APPLICATION OF TAX TO SALES AND LEASES
OF ELECTRIC SIGNS:
REGULATION 1521, CONSTRUCTION CONTRACTORS
REGULATION 1660, LEASES OF TANGIBLE PERSONAL
PROPERTY – IN GENERAL

Staff Recommendation

Staff recommends: 1) Regulation 1521 be amended to tax sales of on-premise electric signs furnished and installed by the seller on 33% of the total selling price, and 2) No change to the current provisions of Regulation 1660, which require property tax reimbursements and mandatory charges for maintenance and insurance to be included as part of taxable lease receipts.

Alternative 1:

Industry agrees with staff's proposed amendment to Regulation 1521. However, industry proposes that Regulation 1660 be amended to exclude property tax reimbursements and charges for maintenance and insurance from taxable lease receipts.

Background, Methodology, and Assumptions**Staff Recommendation:**

The staff recommendation would amend Regulation 1521 to tax sales of on-premise electric signs furnished and installed by the seller on 33% of the total selling price, net of separately stated transportation charges. The Sales and Use Tax Department (SUTD), based on information reported by a number of electric sign companies on sales and use tax returns and discussions with industry, has determined that, on average, tax is being collected on 33% of the total selling price of on-premise electric signs furnished and installed by the seller. While there might be a change in the amount of tax collected on individual sales, there would not be any overall revenue impact from this proposal.

Alternative 1:

Alternative 1 would amend Regulation 1660 to specifically exclude from taxable lease receipts for on-premise electric signs charges for real property taxes whether assessed directly against the lessee or against the lessor, and mandatory charges for maintenance and insurance when mandated by provisions of the federal Internal Revenue Code.

Based on discussions with industry, total lease revenues for electric signs in California are estimated to be approximately \$3 million annually. Property tax and mandated insurance and maintenance charges vary from about 33% to 50% of the lease revenues. If we assume that the average is 40%, total charges for property taxes and mandatory insurance and maintenance would amount to \$1.2 million annually. Sales and use tax revenues on this amount would be \$95,000 annually.

Revenue Summary**Staff Recommendation:**

The staff recommendation has no revenue effect.

Alternative 1:

The revenue impact from amending Regulation 1660 to exclude real property tax reimbursements and mandatory charges for maintenance and insurance from taxable lease receipts would be as follows:

	<u>Revenue Effect</u>
State loss (5%)	\$ 60,000
Local loss (2.25%)	27,000
Transit loss (0.67%)	8,000
Total	\$ 95,000

Preparation

This revenue estimate was prepared by David E. Hayes, Statistics Section, Agency Planning and Research Division. This revenue estimate was reviewed by Ms. Laurie Frost, Chief, Agency Planning and Research Division and Ms. Freda Orendt-Evans, Program Planning Manager, Sales and Use Tax Department. For additional information, please contact Mr. Hayes at (916) 445-0840.

Exhibit 2

Application of Tax to Sales and Leases of On-Premise Electric Signs
Comparison of Current Regulations and Amendments Proposed by Staff and Industry
Regulation 1521, *Construction Contractors* and
Regulation 1660, *Leases of Tangible Personal Property – In General*
Current as of 12/22/99

Action Item	Current Regulatory Language	Staff's and Industry's Proposed Regulatory Language	Comments on Proposed Amendments
Action 1	<p>Regulation 1521</p> <p>(c) Particular Applications</p> <p>(12) <i>No current language. This is a new subdivision.</i></p>	<p>Regulation 1521, (c) Particular Applications</p> <p><u>(12) On-Premise Electric Signs</u></p> <p><u>(A) An on-premise electric sign is any electrically powered or illuminated structure, housing, sign, device, figure, statuary, painting, display, message, placard, or other contrivance or any part thereof affixed to real property and intended or used to advertise, or to provide data or information in the nature of advertising, for any of the following purposes: 1) To designate, identify, or indicate the name or business of the owner or occupant of the premises upon which the advertising display is located, and 2) To advertise the business conducted, services available or rendered, or the goods produced, sold, or available for sale, upon the property where the advertising display has been erected.</u></p> <p><u>(B) Application of tax. An on-premise electric sign is a fixture. Notwithstanding the provisions of 1521(b)(2)(B), operative October 1, 2000, tax applies to 33 percent of the lump-sum sales price for on-premise electric signs that are furnished and installed by the seller. "Sales price" includes charges for materials, fabrication labor, installation labor, overhead, profit, and other charges associated with the sale and installation of the sign. If a contract provides that a contractor is to install an on-premise electric sign furnished by a third party, the charges for installation are not taxable. If a seller furnishes but does not install an on-premise electric sign, the seller is a retailer of the sign and tax applies to the total selling price.</u></p> <p><u>Separately stated charges for transportation are subject to tax as defined in Regulation 1628, <i>Transportation Charges</i>.</u></p>	<p>Industry and staff agree on the proposed revision to Regulation 1521.</p>

Exhibit 2

Application of Tax to Sales and Leases of On-Premise Electric Signs
Comparison of Current Regulations and Amendments Proposed by Staff and Industry
Regulation 1521, Construction Contractors and
Regulation 1660, Leases of Tangible Personal Property – In General
Current as of 12/22/99

Action Item	Current Regulatory Language (Recommended by Staff)	Industry's Proposed Regulatory Language	Comments on Proposed Amendments
Action 2	<p>Regulation 1660</p> <p>(d) Particular Applications.</p> <p>(6) Neon Signs. A lease of a neon sign that is personal property is subject to the provisions of the Sales and Use Tax Law as any other lease of personal property.</p>	<p>Regulation 1660, (d) Particular Applications</p> <p>(6) Neon On-Premise Electric Signs. <u>An on-premise electric sign is any electrically powered or illuminated structure, housing, sign, device, figure, statuary, painting, display, message, placard, or other contrivance or any part thereof affixed to real property and intended or used to advertise, or to provide data or information in the nature of advertising, for any of the following purposes: 1) To designate, identify, or indicate the name or business of the owner or occupant of the premises upon which the advertising display is located, and 2) To advertise the business conducted, services available or rendered, or the goods produced, sold, or available for sale, upon the property where the advertising display has been erected. On-premise electric signs are tangible personal property.</u></p> <p>A lease of an neon on-premise electric sign that is personal property, <u>including neon signs,</u> is subject to the provisions of the Sales and Use Tax Law as any other lease of personal property <u>except, operative October 1, 2000, the measure of tax does not include amounts paid for personal property taxes on the leased property or amounts paid to the lessor for insuring or maintaining the leased property.</u></p>	<p>Staff is of the opinion that Section 6011 of the R&T Code does not provide an exclusion from gross receipts for property taxes or other payments not specifically excluded by statute.</p>

Electric Sign Companies
Summary of Reported Sales - 1998
Percent of Gross Receipts - Taxable

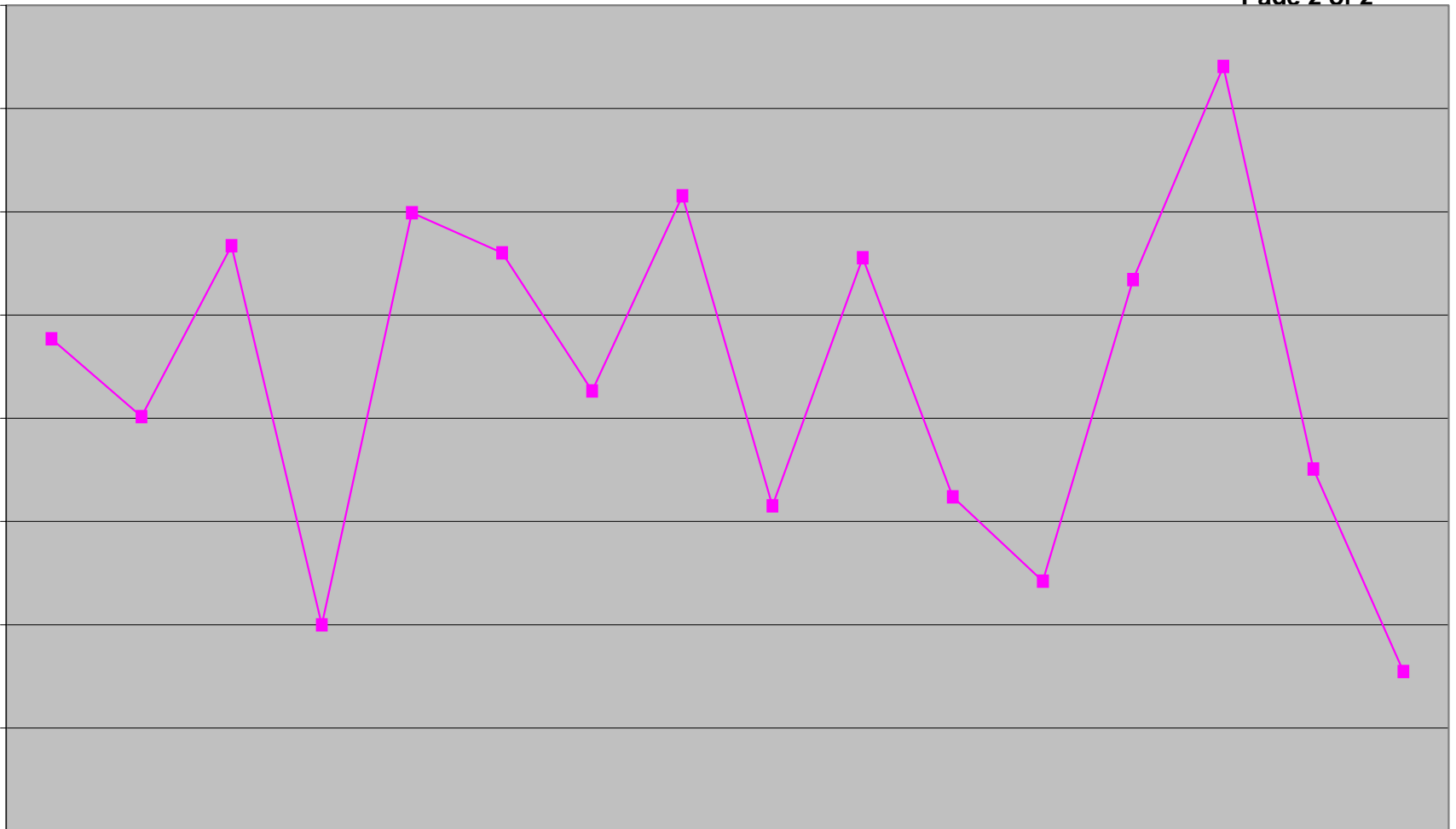
<u>Description</u>	<u>Total Gross Receipts</u>	<u>Exemptions:</u>					<u>Total</u>	<u>Net Taxable Sales</u>	<u>Reported Taxable Pct.</u>
		<u>Resales</u>	<u>Labor</u>	<u>Federal</u>	<u>O/S</u>	<u>Other</u>			
Unadjusted	57812096	2329757	26236605	0	10044062	359477	38969901	18842195	32.59%
Adjusted	45078800	0	26236605	0	0	0	26236605	18842195	41.80%

Sign Companies Sample

Exhibit 3
Page 2 of 2

Pct. of Gross Rcpts. Taxable

80.00%
70.00%
60.00%
50.00%
40.00%
30.00%
20.00%
10.00%
0.00%



—■ Reported & Adj.

1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16
47.70%	40.15%	56.70%	19.99%	59.90%	56.01%	42.65%	61.56%	31.50%	55.55%	32.39%	24.22%	53.44%	74.07%	35.08%	15.47%

Regulation 1521. Construction Contractors.

Reference: Sections 6006 - 6010, 6012, 6012.2., 6012.6, 6012.8, 6012.9, 6015, 6016, 6016.3, 6016.5, 6055, 6091-6095, 6203.5, 6241-6246, 6276, 6276.1, 6379, 6384, 6386, 6421, 6901.5, Revenue and Taxation Code.

(a) Definitions.

(1) Construction Contract.

(A) "Construction contract" means and includes a contract, whether on a lump sum, time and material, cost plus, or other basis, to:

1. Erect, construct, alter, or repair any building or other structure, project, development, or other improvement on or to real property, or

2. Erect, construct, alter, or repair any fixed works such as waterways and hydroelectric plants, steam and atomic electric generating plants, electrical transmission and distribution lines, telephone and telegraph lines, railroads, highways, airports, sewers and sewage disposal plants and systems, waterworks and water distribution systems, gas transmission and distribution systems, pipelines and other systems for the transmission of petroleum and other liquid or gaseous substances, refineries and chemical plants, or

3. Pave surfaces separately or in connection with any of the above works or projects, or

4. Furnish and install the property becoming a part of a central heating, air-conditioning, or electrical system of a building or other structure, and furnish and install wires, ducts, pipes, vents, and other conduit imbedded in or securely affixed to the land or a structure thereon.

(B) "Construction contract" does not include:

1. A contract for the sale or for the sale and installation of tangible personal property such as machinery and equipment, or

2. The furnishing of tangible personal property under what is otherwise a construction contract if the person furnishing the property is not responsible under the construction contract for the final affixation or installation of the property furnished.

(2) Construction Contractor. "Construction contractor" means any person who for himself or herself, in conjunction with, or by or through others, agrees to perform and does perform a construction contract. "Construction contractor" includes subcontractors and specialty contractors and those engaged in such building trades as carpentry, bricklaying, cement work, steel work, plastering, drywall installation, sheet metal work, roofing, tile and terrazzo work, electrical work, plumbing, heating, air-conditioning, elevator installation and construction, painting, and persons installing floor coverings, including linoleum, floor tile, and wall-to-wall carpeting, by permanently affixing such coverings to a floor. "Construction contractor" includes any person required to be licensed under the California Contractors' State License Law (Business & Professions Code

Sections 7000 et seq.), and any person contracting with the United States to perform a construction contract, whether such persons are formed or organized under the laws of this state, or another state or country.

(3) United States Construction Contractor. “United States construction contractor” means a construction contractor who for himself or herself, in conjunction with, or by or through others, agrees to perform and does perform a construction contract for the United States Government.

(4) Materials. “Materials” means and includes construction materials and components, and other tangible personal property incorporated into, attached to, or affixed to, real property by contractors in the performance of a construction contract and which, when combined with other tangible personal property, loses its identity to become an integral and inseparable part of the real property. A list of typical items regarded as materials is set forth in Appendix A.

(5) Fixtures. “Fixtures” means and includes items which are accessory to a building or other structure and do not lose their identity as accessories when installed. A list of typical items regarded as fixtures is set forth in Appendix B.

(6) Machinery and Equipment. “Machinery and equipment” means and includes property intended to be used in the production, manufacturing or processing of tangible personal property, the performance of services or for other purposes (e.g., research, testing, experimentation) not essential to the fixed works, building, or structure itself, but which property incidentally may, on account of its nature, be attached to the realty without losing its identity as a particular piece of machinery or equipment and, if attached, is readily removable without damage to the unit or to the realty. “Machinery and equipment” does not include junction boxes, switches, conduit and wiring, or valves, pipes, and tubing incorporated into fixed works, buildings, or other structures, whether or not such items are used solely or partially in connection with the operation of machinery and equipment, nor does it include items of tangible personal property such as power shovels, cranes, trucks, and hand or power tools used to perform the construction contract. A list of typical items regarded as machinery and equipment together with a list of typical items not regarded as machinery and equipment is set forth in Appendix C.

(7) Time and Material Contract. “Time and material contract” means a contract under which the contractor agrees to furnish and install materials or fixtures, or both, and which sets forth separately a charge for the materials or fixtures and a charge for their installation or fabrication.

(8) Lump Sum Contract. “Lump sum contract” means a contract under which the contractor for a stated lump sum agrees to furnish and install materials or fixtures, or both. A lump sum contract does not become a time and material contract when the amounts attributable to materials, fixtures, labor, or tax are separately stated in the invoice.

(b) Application Of Tax.

(1) United States Construction Contractors.

(A) **Materials and Fixtures.** United States construction contractors are consumers of materials and fixtures which they furnish and install in the performance of contracts with the United States Government. Either the sales tax or the use tax applies with respect to sales of tangible personal property (including materials, fixtures, supplies, and equipment) to contractors for use in the performance of such contracts with the United States for the construction of improvements on or to real property in this state. The fact that the contract may provide principally for the manufacture or acquisition of tangible personal property is immaterial. The sales tax, but not the use tax, applies even though the contractor purchases the property as the agent of the United States.

(B) **Machinery and Equipment.** United States contractors are retailers of machinery and equipment furnished in connection with the performance of a construction contract with the United States Government. Tax does not apply to sales of machinery and equipment to United States contractors or subcontractors, provided title to the property passes to the United States before the contractor makes any use of it. Such sales are sales for resale, and the purchasing contractor may issue a resale certificate. A contractor who uses the machinery or equipment before title passes to the United States is the consumer of that machinery or equipment and either sales tax or use tax applies with respect to the sale to or the use by the contractor.

(2) **Construction Contractors Other than United States Construction Contractors.**

(A) **Materials.**

1. **In General.** Construction contractors are consumers of materials which they furnish and install in the performance of construction contracts. Either sales tax or use tax applies with respect to the sale of the materials to or the use of the materials by the construction contractor.

2. **When Contractor is Seller.** A construction contractor may contract to sell materials and also to install the materials sold. If the contract explicitly provides for the transfer of title to the materials prior to the time the materials are installed, and separately states the sale price of the materials, exclusive of the charge for installation, the contractor will be deemed to be the retailer of the materials.

In the case of a time and material contract, if the contractor bills his or her customer an amount for “sales tax” computed upon his or her marked up billing for materials, it will be assumed, in the absence of convincing evidence to the contrary, that he or she is the retailer of the materials.

If the sale occurs in this state, the sales tax applies to the contractor’s (retailer’s) gross receipts from the sale of the materials. If the sale occurs prior to the time the property is brought into this state, the contractor’s (retailer’s) customer is the consumer and his or her use (unless otherwise exempt) is subject to use tax measured by the sales price. The contractor must collect the use tax and pay it to this state.

(B) **Fixtures.**

1. **In General.** Construction contractors are retailers of fixtures which they furnish and install in the performance of construction contracts and tax applies to their sales of the fixtures.

2. Measure of Tax.

a. In General. If the contract states the sale price at which the fixture is sold, tax applies to that price. If the contract does not state the sale price of the fixture, the sale price shall be deemed to be the cost price of the fixture to the contractor.

b. Determining Cost Price. If the contractor purchases the fixtures in a completed condition, the cost price is deemed to be the sale price of the fixture to him or her and shall include any manufacturer's excise tax or import duty imposed with respect to the fixture prior to its sale by the contractor.

If the contractor is the manufacturer of the fixture, the cost price is deemed to be the price at which similar fixtures in similar quantities ready for installation are sold by him or her to other contractors.

If similar fixtures are not sold to other contractors ready for installation, then the cost price shall be deemed to be the amount stated in the price lists, bid sheets or other records of the contractor.

If the sale price cannot be established in the above manner and the fixture is manufactured by the contractor, the cost price shall be deemed to be the aggregate of the following:

- [1] Cost of materials, including such items as freight-in and import duties,
- [2] Direct labor, including fringe benefits and payroll taxes,
- [3] Specific factory costs attributable to the fixture,
- [4] Any manufacturer's excise tax,
- [5] Pro rata share of all overhead attributable to the manufacture of the fixture, and
- [6] Reasonable profit from the manufacturing operations which, in the absence of evidence to the contrary, shall be deemed to be 5 percent of the sum of the preceding factors.

Jobsite fabrication labor and its prorated share of manufacturing overhead must be included in the sale price of the fixture. Jobsite fabrication labor includes assembly labor performed prior to attachment of a component or a fixture to a structure or other real property.

3. Exceptions - Leased Fixtures. In some instances the construction contractor may furnish and install a fixture for a person, other than the owner of the realty, who intends to lease the fixture in place as tangible personal property as provided in Section 6016.3 of the Revenue and Taxation Code and pay tax measured by rental receipts.

In this case the construction contractor may take a resale certificate from the lessor at the time of the transaction and the sale to the lessor will be considered to be a sale for resale. The resale certificate should indicate that the fixture is purchased for resale by the purchaser as tangible personal property under Section 6016.3 of the Revenue and Taxation Code.

(C) Machinery and Equipment.

1. In General. Construction contractors are retailers of machinery and equipment even though the machinery and equipment is furnished in connection with a construction contract. Tax applies to the contractor's gross receipts from such sales.

2. Measure of Tax.

a. In General. Tax applies to the gross receipts from the sale of machinery and equipment furnished and installed by a construction contractor. If the contract calls only for the furnishing and installation of machinery and equipment, tax applies to the total contract price less those charges excludible from gross receipts under Section 6012 of the Revenue and Taxation Code.

b. Lump Sum Contracts - Determining Gross Receipts. If the contract is for a lump sum and includes the furnishing and installation of materials, fixtures, and machinery and equipment, the gross receipts from the sale of the machinery and equipment shall be the price at which similar quantities ready for installation are sold at retail delivered in the market area where the installation takes place.

If there is no such retail price for the machinery and equipment, then the gross receipts shall be determined from the contracts, price lists, bid sheets, or other records of the contractor.

If the gross receipts cannot be established in the above manner and the machinery and equipment is manufactured by the contractor, the gross receipts from the sale shall be the aggregate of the following:

- [1] Cost of materials, including such items as freight-in and import duties,
- [2] Direct labor, including fringe benefits and payroll taxes,
- [3] Specific factory costs attributable to the machinery or equipment,
- [4] Any manufacturer's excise tax,
- [5] Pro rata share of all overhead attributable to the machinery or equipment, including overhead attributable to manufacturing, selling, contracting, and administration, and
- [6] Reasonable profit from the manufacture and sale of the machinery or equipment which, in the absence of evidence to the contrary, shall be deemed to be 5 percent of the sum of the preceding factors.

Jobsite fabrication labor and its prorated share of manufacturing overhead must be included in the sale price of the machinery or equipment. Jobsite fabrication labor includes assembly labor performed prior to attachment of a component or the machinery or equipment to a structure or other real property.

(D) Cost Plus A Fee Contracts. When a contractor enters into a construction contract for a cost plus a fee or time and materials plus a fee, whether the fee is a lump sum or a percentage of costs, the fee is not included in the measure of tax. When the contractor is the manufacturer of the fixtures or machinery and equipment, the "cost price" of the fixtures and the gross receipts from the sale of the machinery and equipment shall be determined in accordance with (B) and (C) above.

(3) Miscellaneous Sales by Contractors. In addition to sales of fixtures and machinery and equipment, tax applies to all retail sales by contractors of tangible personal property, including parts, supplies, tools, construction equipment, buildings severed or to be severed by the contractor, and furniture, including furniture sold with a building, even though the building is sold “in place.”

(4) Permits. Contractors engaged solely in performing construction contracts which do not involve the sale and installation of fixtures and who do not also engage in business as sellers or retailers are not required to hold seller’s permits. However, if a contractor is a seller or retailer because he or she makes sales of fixtures, materials, or machinery and equipment, or other tangible personal property either in connection with or as part of a construction contract, or otherwise, he or she is required to hold a seller’s permit.

(5) Supplies and Tools for Self-Use. Contractors are the consumers of supplies such as oxygen, acetylene, gasoline, acid, thread-cutting oil, and tools and parts for tools, which they use in their business, and the tax applies to the sale of such supplies and tools to contractors.

(6) Exemption Certificates.

(A) Resale Certificates. Contractors holding valid seller’s permits may purchase fixtures and machinery and equipment for resale by issuing resale certificates to their suppliers. They may not purchase materials for resale unless they are also in the business of selling materials.

A contractor cannot avoid liability for sales or use tax on materials or fixtures furnished and installed by him or her by taking a resale certificate from the prime contractor, interior decorators, designers, department stores, or others. However, under the circumstances described in subsection (b)(2)(B)3., a contractor may take a resale certificate for fixtures furnished and installed by him or her for a person other than the owner of the realty.

(B) Exemption Certificates for Out-of-State Use. Sales tax does not apply to sales of tangible personal property to a construction contractor who holds a valid California seller’s permit when the property is used by the contractor outside this state in his or her performance of a contract to improve real property and as a result of such use the property is incorporated into and becomes a part of real property located outside this state. This exemption is available only if at the time of the purchase the contractor certifies in writing to the seller that he or she holds a valid California seller’s permit (giving the number of that permit and identifying the property purchased) and states that the property will be used in the manner stated above. The certificate must be signed by the contractor or an authorized employee. Such a certification may appear in the body of a purchase order which bears the signature of the purchaser. Any certificate given subsequent to the time of purchase will not be recognized.

If the property purchased under a certificate is used by the contractor in any other manner or for any other purpose than stated in the certificate, the contractor shall be liable for sales tax as if he or she were a retailer making a retail sale of the property at the time of such use, and the sale price of the property to him or her shall be deemed the gross receipts from the sale.

(C) Deductions for Tax-Paid Purchases Resold. A contractor may claim a “tax-paid purchases resold” deduction for any property of which he or she is the retailer when he or she has reimbursed his or her vendor for tax which the vendor is required to pay to the State or has paid the use tax with respect to the property, and has resold the property prior to making any use of it. In the event that the contractor sells short ends or pieces which are not used other than in severing them from larger units purchased by him or her and as to which he or she has paid sales tax reimbursement or use tax, he or she may claim the deduction for tax-paid purchases resold, but the amount of the deduction shall not exceed the price at which he or she sells such short ends or pieces.

(c) Particular Applications.

(1) Draperies and Drapery Hardware. Persons who contract to sell and install draperies including drapery hardware, such as brackets, rods, tracks, etc., are retailers of the items which they furnish and install. Tax applies to the entire contract price exclusive of the charge for installation which charge should be separately stated. Installers who furnish drapery hardware or other tangible personal property may accept resale certificates from department stores or other sellers to furnish and install the draperies and drapery hardware.

The department stores or other sellers furnishing resale certificates are required to pay the tax to the state upon their selling price of the draperies and drapery hardware, exclusive of installation charges. The installer should segregate his or her installation charge in order that the department store or other seller may properly segregate its charge attributable to installation for purposes of determining its taxable gross receipts.

(2) Prefabricated Cabinets. A cabinet will be considered to be “prefabricated” and a “fixture” when 90 percent of the total direct cost of labor and material in fabricating and installing the cabinet is incurred prior to affixation to the realty. In determining this 90 percent, the total direct cost of all labor and materials in fabricating the cabinet to the point of installation will be compared to the total direct cost of all labor and materials in completely fabricating and installing the cabinet. If more than one cabinet is fabricated and installed under the contract, each cabinet will be considered separately in determining whether the cabinet is prefabricated.

(3) Prefabricated Buildings. Prefabricated units such as commercial coaches, house trailers, etc., registered with the Department of Motor Vehicles or the Department of Housing and Community Development, are tangible personal property even though they may be connected to plumbing and utilities. A mobilehome which meets or is modified to meet, all applicable building codes and regulations and which is permanently affixed to realty, is an improvement to realty and is not personal property.

A contract to furnish and install a prefabricated or modular building similar in size to, but which is not, a factory-built school building (relocatable classroom) is a construction contract whether the building rests in place by its own weight or is physically attached to realty. It is immaterial whether the building is erected upon or affixed to land owned by the owner of the building or is leased to the landowner or lessee of the land.

Generally, a contract to furnish and install a small prefabricated building, such as a shed or kiosk, which is movable as a unit from its site of installation, is a construction contract only if the building is required to be physically attached to real property by the seller, upon a concrete foundation or otherwise. The sale of such a unit to rest in place by its own weight, whether upon the ground, a concrete slab, or sills or piers, is not a construction contract even though the seller may deliver the unit to its site of use.

Prefabricated or modular buildings which are “factory-built housing” where permanently affixed to the realty are improvements to realty. The manufacturer of factory-built housing who contracts to furnish and install the factory-built housing manufactured by him or her is the consumer of the materials used in building and installing the factory-built housing and the retailer of the fixtures. Tax applies as provided in (b) above.

(4) Factory-Built School Buildings.

(A) General. On and after September 26, 1989, a contract to furnish and install a factory-built school building is not a construction contract but rather is a sale of tangible personal property.

(B) Definitions.

1. “Factory-built School Building.” The term “factory-built school building” (relocatable classrooms) means and includes:

A. for the period September 26, 1989 through September 12, 1990, any building designed to be used as a school building as defined in Sections 39214 and 81165 of the Education Code and so used. A factory-built school building must be designed in compliance with state laws for school construction and approved by the structural safety section in the office of the State Architect. It must be wholly or substantially manufactured at an offsite location for the purpose of being assembled, erected, or installed on a schoolsite.

B. effective September 13, 1990, any building which is designed or intended for use as a school building and is wholly or substantially manufactured at an offsite location for the purpose of being assembled, erected, or installed on a site owned or leased by a school district or a community college district. A factory-built school building must be designed and manufactured in accordance with building standards adopted and approved pursuant to Chapter 4 (commencing with Section 18935) of Part 2.5 of Division 13 of the Health and Safety Code and must be approved by the structural safety section in the office of the State Architect.

The term does not include buildings licensed by either the Department of Motor Vehicles or the Department of Housing and Community Development. The term also does not include prefabricated or modular buildings which are similar in size to, but which are not, “factory-built school buildings”. It is immaterial whether the building is erected upon or affixed to land owned by the owner of the building or is leased to the landowner or lessee of the land.

2. “Consumer.”

A. For the period September 26, 1989 through September 12, 1990, the term “consumer” as used herein means either (1) a school or a school district or (2) a contractor who purchases a factory-built school building for the purpose of fulfilling the requirements of an existing contract with a school or school district to furnish and install such building.

B. Effective September 13, 1990, the term “consumer” as used herein means either (1) a school district or a community college district or (2) a contractor who purchases a factory-built school building for the purpose of fulfilling the requirements of an existing contract with a school district or a community college district to furnish and install such building.

(C) Place of Sale. The place of sale or purchase of a factory-built school building is the place of business of the retailer regardless of whether the sale of the building includes installation or whether the building is placed upon a permanent foundation.

(D) Application of Tax.

1. Tax applies to 40 percent of the sales price of the building to the consumer excluding any charges for placing the completed building on the site. The sales price of the building shall include amounts representing tangible personal property installed in the building by a subcontractor, whether prior to or after installation of the building at the site, provided such installation is called for in the prime contract for the building. A separate contract to furnish and install tangible personal property in a factory-built school building after installation of the building at the site is a construction contract and tax applies as in (b) above. Any contract or subcontract for site preparation (e.g., foundation) is a construction contract and tax applies as in (b) above.

2. The sale of a factory-built school building to a purchaser who will resell the building without installation is a sale for resale and the seller may accept a resale certificate from the purchaser. If the purchaser then sells to a contractor who has an existing contract to install the building on a school site, tax will apply as in (c)(4)(D)l. above. If tax has been paid on the purchase price of a factory-built school building which is subsequently resold for installation, a tax-paid purchases resold deduction may be taken as provided in Regulation 1701 (18 CCR 1701).

(E) Exclusion Certificate. For the period September 26, 1989, through September 12, 1990, if the purchaser certifies in writing to the retailer that the factory built school building purchased will be consumed in a manner or for a purpose entitling the retailer to exclude 60% of the gross receipts or sales price from the measure of tax and uses the property in some other manner or for some other purpose, the purchaser shall be liable for payment of tax measured by 60% of the sales price. For the above stated period, all retailers who make retail sales of “factory-built school buildings” claimed to be subject to tax measured by 40 percent of the sales price must obtain from the “consumer” a signed certificate substantially in the form set forth below.

**CLAIM FOR 60% EXCLUSION FROM TAX ON
PURCHASE OF FACTORY-BUILT SCHOOL BUILDINGS
(Sec. 6012.6, Rev. & Tax. Code)**

I hereby certify that the factory-built school building that I

(Name of Purchaser-Consumer)

am purchasing under the authority of this certificate from

(Name of Retailer)

will be used as a school building as defined in Sales and Use Tax Regulation 1521. My seller's permit number, if any, is _____.

I further certify that I understand and agree that if the property purchased under the authority of this certificate is used by the purchaser for any purpose other than indicated above, the purchaser shall be liable for payment of tax to the State Board of Equalization at the time of such use measured by 60% of the sales price of the factory-built school building.

Signed by _____
(Name of Purchaser)

As: _____
(Owner, Partner, Purchasing Agent, etc.)

Date _____

(5) Mobilehomes Installed for Occupancy as Residences. Operative July 1, 1980, a special measure of sales or use tax is provided for a mobilehome sold to be affixed to realty for occupancy as a residence.

A mobilehome dealer who sells a new mobilehome to a construction contractor to be affixed to land for occupancy as a residence is the "retailer-consumer" of the property and is required to pay tax for the period in which the sale was made by the dealer measured by an amount equal to 75 percent of the retailer-consumer's purchase price of the mobilehome.

A construction contractor who withdraws a new mobilehome from an inventory purchased for resale to be affixed to realty for occupancy as a residence in the performance of a construction contract is required to pay tax measured by 75 percent of the purchase price by his or her mobilehome vendor except where the purchase is made directly from a mobilehome manufacturer. In the absence of satisfactory evidence of the vendor's purchase price it shall be presumed that the measure of tax for the transaction is an amount equivalent to 60 percent of the sales price of the mobilehome to the construction contractor.

A mobilehome manufacturer who sells a new mobilehome directly to a construction contractor for installation to real property for occupancy as a residence is required to pay tax measured by 75

percent of the sales price at which a similar mobilehome ready for installation would be sold by the manufacturer to a retailer-consumer in this state. A construction contractor who withdraws a new mobilehome from an inventory purchased from a manufacturer for resale must pay tax measured by 75 percent of his or her purchase price.

A mobilehome manufacturer who performs a construction contract by permanently affixing a new mobilehome to real property is the consumer of the material and the retailer of fixtures installed by him or her and the tax applies as set forth in paragraph (b) above.

Reference should also be made to the provisions of Regulation 1610.2 for additional interpretative rules relating to custom additions to the mobilehome prior to sale, transfers of nonvehicle items, and the application of the tax to a purchase made from an out-of-state retailer.

(6) Repair Contracts. A contract to repair a fixture in place or a fixture the contractor is required by the contract to reaffix to the realty is a construction contract. Sales or use tax applies to the gross receipts or sales price of the parts sold by a contractor who is a retailer under this provision. Either sales tax or use tax applies to the sales price of the parts sold to or used by a contractor who is a consumer under this provision.

(A) United States Construction Contractors. A United States construction contractor is the consumer of the parts furnished in the performance of a construction contract to repair a fixture.

(B) Construction Contractors Other Than United States Construction Contractors.

1. A contractor is the retailer of the parts furnished in the performance of a construction contract to repair a fixture when the sale price of the parts is billed separately from the repair labor.

2. A contractor is the consumer of the parts furnished in the performance of a lump sum construction contract to repair a fixture.

(7) Elevator Installations. A large number of components are included in the installation of an elevator system. Those portions constituting the cage or platform and its hoisting machinery are fixtures. The balance of the installation, if attached to a structure or other real property will generally be "materials."

Similarly, installation of escalators and moving sidewalks are in part fixtures and in part materials.

Following are examples of components constituting part of the cage or platform and its hoisting machinery, and which are fixtures:

alarm bell	door operator on cab or car	power units and control boxes
cab or car	door safety edge on cab	pumps
car doors	door sills on cab	pushbuttons on cab
car platform and sling	electronic door protector	wire and piping (which are
door hanger on cab	jack assembly	components of a fixture)
door openers	motors	

Following are examples of components constituting “materials” when attached to realty:

car guides	hoistway door sills and jams	sound insulating panels on materials”
casing section of jack assembly	hoistway door supports	structural steel (unless part of cab, car, or other “fixture”)
guide rails	hoistway entrance	hoistway doors
pushbuttons on hoistway	valve strainer	
hoistway door frames	rail buckets	wire and piping attached to
hoistway door safety edge	sill, struts	“materials”

Following are examples of components constituting parts of escalators or moving sidewalks which are fixtures:

staircase	chains	other operating mechanisms
moving sidewalk		sprockets
moving handrails		motors

(8) Telephone Switchboards and Instruments. Telephone switching equipment installed in a building specifically designed to accommodate the equipment or attached to a building or structure in a manner such that its removal would cause damage to the equipment or building in which it is installed will be considered to be “fixtures” under paragraph (a)(5) of this regulation.

Telephone handsets, modular switching equipment and standardized, off-shelf, general purpose switching equipment sold for use in general purpose office buildings constitute machinery and equipment under paragraph (a)(6) of this regulation. Handsets, modular switching equipment and standardized equipment were previously classified as fixtures.

This change in classification shall be applied prospectively only with respect to construction contracts entered into on and after July 1, 1988, by contractors other than United States construction contractors.

(9) Deep-Well Agricultural Pumps. A deep-well agricultural pump is tangible personal property if installed so that it rests in position by force of gravity and is not otherwise affixed to the land.

The pump is a fixture if:

- (A) It is affixed to the land such as by concrete, bolts or screws,
- (B) It is physically connected to an irrigation system such as by pipes or couplings so as to become an integral part of the system, or
- (C) It is enclosed by a pump house or other building or structure .

(10) Remote Control Garage Door Openers. Remote control garage door opening units are fixtures. Portable transmitter units furnished pursuant to a construction contract are deemed to be fixtures and are taxable as provided in subdivision (b)(2)(B). Sales of portable transmitter units not a part of a construction contract, as, for example, sales of replacement units, are retail sales of tangible personal property and subject to tax as such.

(11) Excess Reimbursement. The excess tax reimbursement provisions of Regulation 1700 apply to construction contractors.

(12) On-Premise Electric Signs

(A) An on-premise electric sign is any electrically powered or illuminated structure, housing, sign, device, figure, statuary, painting, display, message, placard, or other contrivance or any part thereof affixed to real property and intended or used to advertise, or to provide data or information in the nature of advertising, for any of the following purposes: 1) To designate, identify, or indicate the name or business of the owner or occupant of the premises upon which the advertising display is located, or 2) To advertise the business conducted, services available or rendered, or the goods produced, sold, or available for sale, upon the property where the advertising display has been erected.

(B) Application of tax. An on-premise electric sign is a fixture. Notwithstanding the provisions of 1521(b)(2)(B), operative October 1, 2000, tax applies to 33 percent of the sales price of on-premise electric signs that are furnished and installed by the seller. "Sales price" includes charges for materials, fabrication labor, installation labor, overhead, profit, and other charges associated with the sale and installation of the sign. If a contract provides that a contractor is to install an on-premise electric sign furnished by a third party, the charges for installation are not taxable. If a seller furnishes but does not install an on-premise electric sign, the seller is a retailer of the sign and tax applies to the total selling price.

Separately stated charges for transportation are subject to tax as defined in Regulation 1628, *Transportation Charges*.

Appendix A The following is a list of typical items regarded as materials:

Asphalt	Linoleum	Steel
Bricks	Lumber	Stone
Builders' hardware	Macadam	Stucco
Caulking material	Millwork	Tile
Cement	Mortar	Wall coping
Conduit	Oil	Wallboard
Doors	Paint	Wallpaper
Ducts	Paper	Wall-to-wall carpeting
Electric wiring and connections	Piping, valves, and pipe fittings	(when affixed to the floor)
Flooring	Plaster	Weather stripping
Glass	Power poles, towers, and lines	Windows
Gravel	Putty	Window screens
Insulation	Reinforcing mesh	Wire netting and screen
Lath	Roofing	Wood preserver
Lead	Sand	
Lime	Sheet metal	

Appendix B The following is a list of typical items regarded as fixtures:

Air conditioning units	Furnaces, boilers, and heating units
Awnings	Lighting fixtures
Burglar alarm and fire alarm fixtures	Plumbing fixtures
Cabinets, counters, and lockers (prefabricated)	Refrigeration units
Cranes ¹ (including moving parts of cranes) affixed or annexed to a building, structure or fixed work	Signs
Electric generators (affixed to and accessory to a building, structure or fixed works)	Television antennas
Elevators, hoists, and conveying units	Transformers and switchgear
	Vault doors and equipment
	Venetian blinds

¹Moving parts of cranes are classified as machinery and equipment when furnished and installed pursuant to fixed price construction contracts entered into prior to July 1, 1985.

Appendix C The following are lists of typical items regarded as:

Machinery and Equipment	Not Machinery or Equipment
Drill presses	Fixtures and materials as defined in this regulation
Electric generators (unaffixed, or, if affixed, which meet the requirements of subparagraph (a)(6))	Wiring, piping, etc., used as a source of power, water, etc., for machinery and equipment
Lathes	Radio transmission antennas
Machine tools	Large tanks (i.e., over 500 barrel capacity)
Printing presses	Fire alarm systems
units	Street light standards
	Cooling towers other than small prefabricated cooling

History: Effective July 1, 1939.

Adopted as of January 1, 1945, as a restatement of previous rulings.

Amended September 2, 1965, applicable as amended September 17, 1965.

Amended and renumbered November 3, 1971, effective December 3, 1971.

Amended February 4, 1976, effective April 1, 1976. Rewrote and expanded regulation for clarity, combined Regulation 1615, added particular applications, and applied Regulation 1521 definition of “fixture” to U. S. Contractors.

Amended August 17, 1976, effective September 19, 1976. Clarified “U. S. Government,” limited exemption certificate, and clarified “generators” in appendices.

Amended December 7, 1978, effective February 18, 1979. Subsections (a)(3), (b)(1)(A), and (b)(1)(B) no longer reference instrumentalities of the United States; subsection (b)(1)(A) was amended to apply sales tax to the sale of tangible personal property to contractors for use on construction contracts with the United States; amends subsection (c)(7) to provide that the section only applies to transactions prior to 1/1/79.

Amended August 1, 1980, effective August 22, 1980, operative July 1, 1980. On first page, added (c)(4) and renumbered following subsections: in (c)(3), first sentence, deleted “mobilehomes” and substituted “commercial coaches”; in third paragraph, deleted “as defined in Regulation 1521.2,” from first sentence, and deleted second sentence; added (c)(4), and renumbered following sections.

Amended November 19, 1980, effective January 16, 1981. In (c)(3) corrected typographical error. In (c)(4), third paragraph, substituted “construction contractor” for “any person”; added “in the performance of a construction contract,” and added exception for purchases made directly from a mobilehome manufacturer; substituted “construction contractor” for “person withdrawing and affixing the property to realty,”. In fourth paragraph, added provision regarding withdrawal by construction contractor of new mobilehome from inventory purchased from a manufacturer.

Amended December 1, 1983, effective April 14, 1984. In (c)(3) added reference to the Department of Housing and Community Development. In (c) added new (c)(8) and renumbered former (c)(8) to (c)(9); deleted former text and added reference to Regulation 1700. Deleted former subdivision (d). In appendix C changed reference to subparagraph (a)(6).

Amended February 5, 1986, effective May 11, 1986. Deletes the term “Moving parts of cranes” as machinery and equipment under Appendix C and adds the term “Cranes” to Appendix B as fixtures with a footnote that moving parts of cranes are classified as machinery and equipment when furnished and installed pursuant to fixed price construction contracts entered into prior to July 1, 1985.

Amended May 3, 1988, effective July 2, 1988. Added subdivision (c)(7) to make clear and specific that certain types of telephone equipment are classified as “fixtures” whereas other types of telephone equipment are classified as “machinery and equipment”. In Appendix B, deleted reference to “telephone switchboards and instruments”.

Amended April 5, 1989, effective June 17, 1989. The change to subdivision (c)(3) provides that construction contracts include contracts to furnish and install a relocatable classroom, or other prefabricated or modular building of similar size, whether the building rests in place by its own weight or is physically attached to the realty. The revised subdivision also provides that a contract to furnish and install a small prefabricated building such as a shed or kiosk, which is moveable from its installation site, is a construction contract only if the building is required to be physically attached to the realty by the seller.

Amended June 5, 1991, effective August 18, 1991. Modified the definition of the term “factory-built school building” and deleted the provisions relating to the liability of the purchaser for taxes if the building is used for some purpose other than a school. Amended paragraph (c)(3) to remove reference to factory-built school buildings (relocatable classrooms). Added paragraph (c)(4).

Amended February 8, 1995, effective July 16, 1995. Amended subparagraph (c)(6) to include, as subparagraphs (A) and (B), specific examples of how tax applies to both United States contractors and other construction contractors when performing repair construction contracts. Deleted gender-based language from

subparagraphs (a)(2) & (3), (b)(2)(A)2., (b)(2)(B)2.b., (b)(4), (b)(6), (c)(3), and (c)(5). Corrected clerical errors in (c)(3) and (c)(4)(E).

Amended November 18, 1998, effective February 13, 1999. Subdivision (a)(2) amended by adding sentence “Construction contractor` ... country.”

Regulation 1660. Leases of Tangible Personal Property - In General.

Reference: Sections 6006, 6006.1, 6006.3, 6006.5, 6009, 6010, 6010.1, 6010.65, 6011, 6012, 6012.6, 6016.3, 6092.1, 6094, 6094.1, 6243.1, 6244, 6244.5, 6379, 6390, 6391, 6407, and 6457, Revenue and Taxation Code.

(a) Definitions.

(1) Lease. The term “lease” includes rental, hire, and license. It includes a contract under which a person secures for a consideration the temporary use of tangible personal property which, although not on his or her premises, is operated by, or under the direction and control of, the person or his or her employees. “Lease,” however, does not include a use of tangible personal property for a period of less than one day for a charge of less than twenty dollars (\$20) when the privilege to use the property is restricted to use thereof on the premises or at a business location of the grantor of the privilege (see (e) below).

(2) Sale Under a Security Agreement.

(A) Where a contract designated as a lease binds the “lessee” for a fixed term and the “lessee” is to obtain title at the end of the term upon completion of the required payments or has the option to purchase the property for a nominal amount, the contract will be regarded as a sale under a security agreement from its inception and not as a lease. The option price will be regarded as nominal if it does not exceed \$100 or 1 percent of the total contract price, whichever is the lesser amount.

(B) In the case of a contract designated as a lease with any state or local government, the governmental agency designated as a lessee shall be treated as bound for a fixed term notwithstanding any right it may have to terminate the contract to the extent that sufficient funds are not appropriated to pay amounts due under the contract. Such transactions are subject to tax as sales under a security agreement at their inception.

(3) Sale and Leaseback Transactions.

(A) General. Transactions structured as sales and leasebacks will be treated as financing transactions if (1) the “lease” transaction would be regarded as a sale at inception under paragraph (a)(2) of this regulation, (2) the purchaser-lessor does not claim any deduction, credit or exemption with respect to the property for federal or state income tax purposes, and (3) the amount which would be attributable to interest, had the transaction been structured originally as a financing agreement, is not usurious under California law. Transactions treated as financing transactions are not subject to sales or use tax.

(B) Special Application. Transactions structured as sales and leasebacks will also be treated as financing transactions if all of the following requirements are met:

1. The initial purchase price of the property has not been completely paid by the seller-lessee to the equipment vendor.

2. The seller-lessee assigns to the purchaser-lessor all of its right, title and interest in the purchase order and invoice with the equipment vendor.

3. The purchaser-lessor pays the balance of the original purchase obligation to the equipment vendor on behalf of the seller-lessee.

4. The purchaser-lessor does not claim any deduction, credit or exemption with respect to the property for federal or state income tax purposes.

5. The amount which would be attributable to interest, had the transaction been structured originally as a financing agreement, is not usurious under California law.

6. The seller-lessee has an option to purchase the property at the end of the lease term, and the option price is fair market value or less.

(C) Tax Benefit Transactions. Tax does not apply to sale and leaseback transactions entered into in accordance with former Internal Revenue Code Section 168(f)(8), as enacted by the Economic Recovery Tax Act of 1981 (Public Law 97-34).

(D) Acquisition Sale and Leaseback Transactions. No sales or use tax applies to the transfer of title to, or the lease of, tangible personal property pursuant to an acquisition sale and leaseback, which is a transaction satisfying all of the following conditions:

1. The seller/lessee has paid California sales tax reimbursement or use tax with respect to that person's purchase of the property.

2. The acquisition sale and leaseback is consummated within 90 days of the seller/lessee's first functional use of the property (this ninety day period does not begin to run until the first functional use of the property; a period of storage after the purchase but before the first functional use is not used to calculate the 90 day period).

3. The acquisition sale and leaseback transaction is consummated on or after January 1, 1991.

The sale of the property at the end of the lease term is subject to sales or use tax. Any lease of the property by the purchaser/lessor to any person other than the seller/lessee would be subject to use tax measured by rentals payable. A lease to the seller/lessee at the end of the original lease term is subject to use tax measured by rentals payable unless such lease is pursuant to an election to exercise an option to extend the lease term, which option was contained in the original lease agreement.

(b) Leases as Sales or Purchases.

(1) In General. Any lease of tangible personal property in any manner whatsoever for a consideration is a “sale” as defined in section 6006 of the Revenue and Taxation Code, and a “purchase” as defined in section 6010 of the Revenue and Taxation Code, except a lease of:

(A) Motion picture films and video tapes, including television films and video tapes, whether or not they are productions complete in themselves. See, however, subdivision (d)(2) below for application of tax for periods on and after September 1, 1983, to leases of video cassettes, videotapes, and videodiscs for private use under which the lessee or renter does not obtain or acquire the right to license, broadcast, exhibit, or reproduce the video cassette, videotape, or videodisc.

(B) Linen supplies and similar articles, including such items as towels, uniforms, coveralls, shop coats, dust cloths, caps and gowns, etc., when an essential part of the lease is the furnishing of the recurring service of laundering or cleaning of the articles leased.

(C) Household furnishings with a lease of the living quarters in which they are to be used. The lessor of the household furnishings must also be the lessor of the living quarters. The living quarters must be real property rather than tangible personal property.

(D) Mobile transportation equipment for use in transportation of persons or property (see regulation 1661 (18 CCR 1661)).

(E) Tangible personal property leased in substantially the same form as acquired by the lessor or leased in substantially the same form as acquired by a transferor as to which the lessor or his or her transferor acquired the property in a transaction that was a retail sale with respect to which the lessor or the transferor has paid sales tax reimbursement or as to which the lessor or the transferor has timely paid use tax measured by the purchase price of the property.

As used herein, “transferor” means:

1. A person from whom the lessor acquired the property in a transaction described in section 6006.5(b) of the Revenue and Taxation Code, or
2. A decedent from whom the lessor acquired the property by will or by law of succession.

For purposes of 1. above, the transaction will qualify if the property is acquired in a transfer of all or substantially all of the tangible personal property held or used by the transferor in all of his or her activities requiring the holding of a seller’s permit or permits or in an activity or activities not requiring the holding of a seller’s permit or permits, and the ownership of the tangible personal property is substantially similar after the transfer.

(F) Tangible personal property occurring on or after January 1, 1997 described in sections 17053.49 or 23649 of the Revenue and Taxation Code by the manufacturer of that property when leased to a qualified person, as described in sections 17053.49 or 23649 of the Revenue and

Taxation Code, in a form not substantially the same as acquired as to which the manufacturer made a timely election to report and pay tax measured by the cost price of that property as defined in section 6244.5 of the Revenue and Taxation Code and Regulation 1525.3.

(G) A mobilehome, as defined in sections 18008(a) and 18211 of the Health and Safety Code, other than a mobilehome originally sold new prior to July 1, 1980 and not subject to local property taxation.

(2) Leases as Continuing Sales and Purchases. In the case of any lease that is a “sale” and “purchase” under (1) above, the granting of possession by the lessor to the lessee, or to another person at the direction of the lessee, is a continuing sale in this state by the lessor, and the possession of the property by a lessee, or by another person at the direction of the lessee, is a continuing purchase for use in this state by the lessee, as respects any period of time the leased property is situated in this state, irrespective of the time or place of delivery of the property to the lessee or such other persons. The application of tax to such leases is set forth below .

(c) General Application of Tax.

(1) Nature of Tax. In the case of a lease that is a “sale” and “purchase” the tax is measured by the rentals payable. Generally, the applicable tax is a use tax upon the use in this state of the property by the lessee. The lessor must collect the tax from the lessee at the time rentals are paid by the lessee and give him or her a receipt of the kind called for in regulation 1686 (18 CCR 1686). The lessee is not relieved from liability for the tax until he or she is given such a receipt or the tax is paid to the state.

When the lessee is not subject to use tax (for example, insurance companies), the sales tax applies. The sales tax is upon the lessor and is measured by the rentals payable.

Neither the sales tax nor the use tax applies to leases to the United States and its instrumentalities unless federal law permits taxing the instrumentality. For a more complete explanation regarding sales to the United States and its instrumentalities see Regulation 1614 (18 CCR 1614).

The “rentals” subject to the tax include any payments required by the lease, including amounts paid for personal property taxes on the leased property, whether assessed directly against the lessee or against the lessor, but do not include amounts paid to the lessor for:

(A) Collection costs, including attorney’s fees, court costs, repossession charges, and storage fees; but tax does apply to any delinquent rental payments, including those collected by court action;

(B) Insuring, repairing or refurbishing the leased property following a default;

(C) Cost incurred in defending a court action or paying a tort judgment arising out of the lessee's operation of the leased property, or any premiums paid on insurance policies covering such court actions or tort judgments;

(D) Cost incurred in disposing of the leased property at expiration or earlier termination of the lease;

(E) Late charges and interest thereon for failing to pay the rentals timely;

(F) Separately stated optional insurance charges, maintenance or warranty contracts.

(2) **Property Leased in Form Acquired.** No sales or use tax is due with respect to the rentals charged for tangible personal property leased in substantially the same form as acquired by the lessor, or by his or her transferor, as to which the lessor or transferor has paid sales tax reimbursement or has paid use tax measured by the purchase price. If such tax has not been so paid, and the lessor desires to pay tax measured by the purchase price, it must be reported and paid timely with the return of the lessor for the period during which the property is first placed in rental service. A timely return is a return filed within the time prescribed by sections 6452 or 6455 of the Revenue and Taxation Code, whichever is applicable.

(3) **Property Purchased Tax Paid.** In the case of property ultimately leased in substantially the same form as acquired, payment of tax or tax reimbursement measured by the purchase price at the time the property is acquired constituted an irrevocable election not to pay tax measured by rental receipts. The lessor may not change his or her election by reporting tax on rental receipts and claiming a tax-paid-purchase-resold deduction.

(4) **Property Acquired in Exempt Transactions.**

(A) A purchaser of tangible personal property acquired in a transaction defined as an occasional sale in section 6006.5(a) of the Revenue and Taxation Code and leased in substantially the same form as acquired by him or her, may elect to pay use tax measured by the purchase price of the property in lieu of tax measured by rental receipts.

(B) A purchaser of tangible personal property acquired in a transaction which qualifies under section 6006.5(b) of the Revenue and Taxation Code and leased in substantially the same form as acquired by his or her transferor may elect to pay use tax measured by his or her transferor's purchase price of the property in lieu of tax on rental receipts. This provision has application where the transferor did not pay tax or tax reimbursement when he or she acquired the property.

For purposes of this provision, the transaction will qualify if the property is acquired in a transfer of all or substantially all of the tangible personal property held or used by the transferor in all of his or her activities requiring the holding of a seller's permit or permits or in an activity or activities not requiring the holding of a seller's permit or permits and the ownership of the tangible personal property is substantially similar after the transfer (see also (b)(1)(E) above).

(C) The election provided for in (A) and (B) above shall be exercised by the lessor in a timely return filed for the period in which the property is first leased by him or her.

(5) Property Subleased. Tax does not apply to receipts from subleases of tangible personal property which is leased in substantially the same form as acquired by the prime lessor where the prime lessor has paid sales tax reimbursement or use tax measured by his or her purchase price. Also, tax does not apply to subleases of tangible personal property if the tax is paid on rental receipts derived under the prime lease, or any prior sublease.

(6) Use of Property by Lessor. If a lessor, after leasing property and collecting and paying use tax, or paying sales tax, measured by rental receipts, makes any use of the property in this state, other than incidental use, he or she is liable for use tax measured by the purchase price of the property. He or she may, however, apply as a credit against the tax so computed, the amount of tax previously paid to the board with respect to rentals of the property. If the credit is less than the tax, he or she must pay the difference with his or her return, but may apply the amount of such payment against his or her liability for tax on subsequent rentals of the property. Effective January 1, 1973, through December 31, 1978, any amount collected as tax or tax reimbursement by the lessor from the lessee on such subsequent rentals will be regarded as excess tax reimbursement to the extent that the lessor is permitted by the foregoing provisions to apply the amount of his or her payment for use tax against his or her liability for tax on subsequent rentals of the property. An incidental use, e.g., a brief loan of property which otherwise is leased by the lessor pursuant to leases which are continuing sales, subjects the lessor to liability for use tax measured by the fair rental value of the property during the period of the incidental use. (See Regulation 1669.5(b)(7)(18 CCR 1669.5(b)(7)).)

(7) Options to Purchase. An agreement providing for the lease of tangible personal property and granting the lessee an option to purchase the property results in a sale when the option is exercised. The tax applies to the amount required to be paid by the purchaser upon the exercise of the option.

(8) Tax Paid to Another State. A lessor who leases property in substantially the same form as acquired and who has paid a retail sales or use tax, or reimbursement therefor, imposed with respect to that property by any other state, political subdivision thereof or the District of Columbia prior to leasing the property in this state may credit the payment against any use tax imposed on him or her by this state because of such lease. However, to be entitled to the credit the lessor must make a timely election to measure any tax liability for the property by its purchase price, unless the out-of-state tax equals or exceeds the tax imposed on him or her by this state. If the out-of-state tax equals or exceeds the tax imposed on him or her by this state, the lessor will be deemed to have made a timely election and the rental receipts will not be subject to tax provided the property is leased in substantially the same form as acquired. If a timely election is not made, no credit will be allowed because the tax due will be a use tax measured by rental receipts and imposed directly against the lessee, a person other than the one who paid the out-of-state tax or tax reimbursement. If the lessee is not subject to use tax and the lessor does

not make a timely election to pay tax measured by his or her purchase price, he or she may not credit the amount of the out-of-state tax against the tax due on the rental receipts because the tax due is a sales tax rather than a use tax.

A credit otherwise permitted by the foregoing provisions shall not be allowed against taxes which are measured by periodic payments made under a lease, to the extent that taxes imposed by any other state, political subdivision or the District of Columbia were also measured by periodic payments made under a lease prior to the lease of the property in this state.

(9) Assignment of Leases.

(A) In General-Status of Assigned Leases. The situations described in (B), (C), and (D) below involve existing leases which are “sales” and “purchases” subject to tax measured by rental payments. When such a lease is assigned, whether or not title to the leased property is transferred, the rental payments remain subject to tax, without any option to measure tax by the purchase price. An assignee-purchaser who uses the property after termination of the lease is subject to use tax measured by the purchase price as provided in (c)(6) above.

Generally, when an existing lease that is not a “sale” and “purchase” is assigned, whether or not title to the leased property is transferred, the rental payments are not subject to tax. If title is transferred, tax applies measured by the sales price.

For rules relating to the assignment of leases of mobile transportation equipment coming within the exclusions provided in sections 6006(g)(4) and 6010(e)(4) of the Revenue and Taxation Code, see Regulation 1661 (18 CCR 1661).

(B) Assignment of a Right and Creation of a Security Interest. This type of assignment is an assignment by the lessor of the right to receive the rental payments together with the creation of a security interest in the leased property which is designated as such. The assignee has recourse against the assignor.

The assignee in this situation does not have the rights of a lessor and is not obligated to collect or pay the tax measured by the rental payments. The lessor remains subject to the obligation of collecting and reporting the tax even if he or she does not receive the rental payments directly from the lessee. The assignee, however, is obligated to remit to the board any amounts paid to him or her by the lessee as tax.

If the assignee enforces the security agreement and takes title to the property, the assignee as lessor becomes responsible for collecting and reporting the tax.

(C) Assignment of Contract with Transfer of Right, Title, and Interest for Security Purposes. This type of assignment is an assignment by the lessor of the lease contract together with the transfer of the right, title, and interest in the leased property for security purposes. After the termination of the lease, the property usually reverts to the original lessor. The assignment

contract may specify that the transfer is for security purposes, or the circumstances may otherwise demonstrate it (e.g., a separate agreement that the property will be returned to the assignor at the termination of the lease). The assignee has recourse against the assignor.

In this situation, the assignee has assumed the position of a lessor. He or she is required to hold a seller's permit and is obligated to collect, report and pay the tax to the board. The assignor should obtain a resale certificate, covering the property in question, from the assignee.

(D) Assignment of Contract and All Right, Title, and Interest. This type of assignment is an assignment by the lessor of the lease contract together with the transfer of all right, title, and interest in the leased property. The assignment is not for security purposes, and the assignor does not retain any substantial ownership rights in the contract or the property. The assignee has no recourse against the assignor.

In this situation, the assignee has assumed the position of a lessor. He or she is required to hold a seller's permit and is obligated to collect, report and pay the tax to the board. The assignor should obtain a resale certificate, covering the property in question, from the assignee.

(d) Particular Applications.

(1) Chemical Toilets. A lease of a chemical toilet unit is a sale or purchase and tax applies measured by the lease or rental price regardless of whether the unit is leased in substantially the same form as acquired and regardless of whether sales tax reimbursement or use tax has been paid.

(2) Video Cassettes, Videotapes, Videodiscs. On and after September 1, 1983, the rental or lease of a video cassette, videotape, or videodisc for private use under which the lessee or renter does not obtain or acquire the right to license, broadcast, exhibit, or reproduce the video cassette, videotape, or videodisc is a sale or purchase and tax applies measured by rental receipts. Tax applies measured by rental receipts regardless of whether the property is leased in substantially the same form as acquired and regardless of whether sales tax reimbursement or use tax has been paid by the lessor with respect to the purchase price of the video cassette, videotape, or videodisc. If the property was rented, leased or otherwise used prior to September 1, 1983, no refund, credit, or offset for any sales tax reimbursement or use tax paid on the purchase price will be allowed against the tax measured by the lease or rental price after September 1, 1983.

(3) Lease of an Animal. A lease of any form of animal life of a kind the products of which ordinarily constitute food for human consumption is not subject to tax.

(4) Composed Type, Reproduction Proofs, Impressed Mats. Tax does not apply to leases of composed type or reproduction proofs thereof by a typographer to another person for use in the preparation of printed matter or to leases of such reproduction proofs or impressed mats to a printer or publisher for use in printing, except when the reproduction proof is a component part of a "paste-up," "mechanical" or "assembly."

(5) Repair Parts. Sales tax does not apply to sales of repair parts to a lessor which are used by him or her in maintaining the leased equipment pursuant to a mandatory maintenance contract where the rental receipts are subject to tax. Such repair parts are regarded as being part of the sale of the leased item and may be purchased for resale. The amount paid by the lessee under the mandatory maintenance contract is regarded as part of the rental payments.

(6) Neon-On-Premise Electric Signs. An on-premise electric sign is any electrically powered or illuminated structure, housing, sign, device, figure, statuary, painting, display, message, placard, or other contrivance or any part thereof affixed to real property and intended or used to advertise, or to provide data or information in the nature of advertising, for any of the following purposes: 1) To designate, identify, or indicate the name or business of the owner or occupant of the premises upon which the advertising display is located, or 2) To advertise the business conducted, services available or rendered, or the goods produced, sold, or available for sale, upon the property where the advertising display has been erected. On-premise electric signs are tangible personal property.

A lease of an neon-on-premise electric sign that is personal property, including neon signs, is subject to the provisions of the Sales and Use Tax Law as any other lease of personal property except, operative October 1, 2000, the measure of tax does not include amounts paid for personal property taxes on the leased property or amounts paid to the lessor for insuring or maintaining the leased property.

(7) Property Affixed to Realty. For the purpose of this regulation, “tangible personal property” includes any leased fixture affixed to realty if the lessor has the right to remove the fixture upon breach or termination of the lease agreement, unless the lessor of the fixture is also the lessor of the realty to which the fixture is affixed. The term fixture as used herein has the same meaning as the term “fixture” in regulation 1521 (18 CCR 1521).

Leases of structures together with the component parts of such structures, e.g., plumbing fixtures, air conditioners, water heaters, etc., will be treated as leases of real property. Accordingly, tax applies to contracts to construct such structures and the attached components in accordance with regulation 1521 (18 CCR 1521).

On and after September 26, 1989, leases of factory-built school buildings (relocatable classrooms) as defined in paragraph (c)(4)(B) of Regulation 1521 (18 CCR 1521), “Construction Contractors”, will be treated as leases of real property with the lessor to the school or school district as the consumer. If the lessor is the manufacturer, tax applies to the manufacturer’s costs of all tangible personal property used in constructing the factory-built school building. If the lessor is other than the manufacturer, tax applies to 40% of the sales price of the factory-built school buildings to such lessor.

For purposes of this section, “structure” does not include any prefabricated mobile homes or similar items which are registered with the Department of Motor Vehicles. It also does not include a portable building, such as a shed or kiosk, which is moveable as a unit from its site of

installation, unless the building is physically attached to the realty, upon a concrete foundation or otherwise. Such a building resting in place by its own weight, whether upon the ground, a concrete slab, or sills or piers, is not a "structure." A prefabricated or modular building similar in size to, but which is not, a factory-built school building (relocatable classroom) is a "structure" whether the building rests in place by its own weight or is physically attached to realty.

Those fixtures which are essential to the structure such as heating and air conditioning units, sinks, toilets, and faucets, which are leased by the lessor of the structure to which they are attached are considered part of the structure and therefore improvements to real property.

On the other hand, those fixtures which although being a component part of the structure are leased by other than the lessor of the structure, will be considered tangible personal property. Accordingly, the tax consequences with respect to such fixtures will be the same as with respect to any other lease of tangible personal property.

(8) Mobilehomes.

(A) The leasing of any mobilehome purchased by a retailer without payment of sales tax reimbursement or use tax and first leased prior to July 1, 1980, is a continuing sale and tax is due measured by the periodic lease payments unless the mobilehome becomes subject to local property taxation, in which event the lease of the property is thereafter exempt from the sales and use tax.

(B) The lease of a new mobilehome purchased by a retailer without payment of sales tax reimbursement or use tax and first leased on or after July 1, 1980, is excluded from classification as a continuing sale and the lessor's use of such property by leasing is subject to the use tax.

If the use of the property is for occupancy as a residence then the tax is measured by an amount equivalent to 75 percent of the purchase price paid by the lessor's vendor. In the absence of satisfactory evidence of the vendor's purchase price it shall be presumed that the measure of use tax is an amount equivalent to 60 percent of the sales price of the mobilehome to the lessor unless the vendor is also the manufacturer. If such mobilehome is purchased by the lessor from the manufacturer, the measure of the use tax liability is 75 percent of the purchase price of the mobilehome to the lessor.

If the use of the property is not for occupancy as a residence, then the tax is measured by the full retail sales price to the lessor.

(C) The subsequent lease of a used mobilehome which was first sold new in this state after July 1, 1980, is exempt from the sales and use tax.

(e) Grant of Privilege to Use Which is Not a Lease.

(1) In General. Certain restricted grants of a privilege to use property are excluded from the term “lease.” To fall within the exclusion, the use must be for a period of less than one continuous 24-hour period, the charge must be less than \$20, and the use of the property must be restricted to use on the premises or at a business location of the grantor of the privilege to use the property.

(2) Definitions.

(A) “Grantor of the privilege” means a person who allows another person to use the personal property.

(B) “Use” includes the possession of, or the exercise of any right or power over personal property by a grantee of a privilege to use the property.

(C) “Premises” or “business location” means a building or specific area owned or leased by a grantor or to which a grantor has an exclusive right of use or a space occupied by the personal property which a grantor allows other persons to use in place. For example:

1. A place in a depot at which a grantor places a coin-operated amusement device pursuant to a contract with the management of the depot.

2. An area in an apartment house or motel where a grantor has a right to place coin-operated washing machines and dryers for use by occupants of the apartment house or motel.

3. A laundromat owned or leased by a person who places therein coin-operated washing machines and dryers for use by customers.

4. A riding stable at which horses are furnished to the public at an hourly rate with a restriction that the horses be ridden within a specific area owned or leased by a grantor of the privilege. The “specific area” might be an enclosed arena or other place the exterior boundaries of which are defined by walls, fences or otherwise in such a manner that the area readily can be recognized and distinguished from adjoining or surrounding property.

5. A golf course owned or leased by a golf club which owns or leases golf carts that it furnishes to persons for use in playing the course, or a golf course under the supervision and control of a golf professional who owns or leases golf carts that he or she furnishes to persons for use in playing the course.

(3) Examples of Situations Which Do Not Qualify for Exclusion from the Term “Lease”.

(A) One of several rental firms permitted by a hospital to do so rents a portable television set and stand to a hospital patient for a charge of \$4.00 per day for a period of six days.

This situation does not qualify for the exclusion because the period of “use” is not for less than one day, the total rental is not less than \$20 and the place of use is not the “premises” or “business location” of the rental firm since it does not have “exclusive right of use” of the hospital as regards the placing of its rental units therein nor is the space regularly occupied by it for use in place.

(B) Rental of a canoe for a period of eight hours for a total charge of \$4 when the customer will use the canoe on the Russian River.

This situation does not qualify for the exclusion because the river is not the premises or business location of the grantor of the privilege.

(C) Rental of tools to be used on the premises of the owner of the tools for a period of eight hours invoiced as follows:

1 Portable lamp	\$4
1 Wheel pulley	4
1 Portable hoist	4
1 Sander	4
1 Spray gun	<u>5</u>
Total rental	\$21

This situation does not qualify for the exclusion because the agreement for rental of the property is a single agreement involving rental charges of \$21 and does not meet the requirement that the charge be less than \$20.

(D) An equipment rental firm rents a cement mixer to a customer who takes the mixer to his or her home and uses it for less than one day. The rental charge is \$9. The mixer is of a type which must be firmly “in place” during the cement mixing operation.

This situation does not qualify for the exclusion because although the mixer is firmly “in place” during the mixing operation, it is not in a space regularly occupied by it for use in place by customers of the grantor.

(4) Application of Tax to Situations Qualifying for Exclusion from the Term “Lease”. The grantor of the privilege to use property under the conditions described in (1) above is the consumer of the property. Accordingly, charges by him or her for the privilege to use the property are not subject to tax. Tax applies to the sale of the property to him or her by a retailer or to his or her use of the property, measured by his or her purchase price, when the property is purchased from a retailer in California under a resale certificate or from a retailer at an out-of-state location. If the property is acquired through an “occasional sale” as defined in section 6006.5 of the Revenue and Taxation Code, or other exempt transaction, no tax applies to the acquisition or use of the property by the grantor nor to his or her charges for the privilege to use the property.

History: Amended November 3, 1969, applicable on and after November 10, 1969.
Amended November 5, 1970, effective December 10, 1970.
Amended and renumbered November 3, 1971, effective December 3, 1971.
Amended December 15, 1971, applicable on and after December 15, 1971.
Amended February 16, 1972, effective March 25, 1972.
Amended November 15, 1972, effective December 21, 1972.
Amended June 24, 1976, effective July 30, 1976. In (c)(7) added and defined “incidental use.”
Amended August 17, 1976, effective September 19, 1976. Noted that sales tax on United States or its instrumentalities is legal only when permitted by federal law.
Amended August 17, 1976, effective October 23, 1976. Added part of (c)(1) previously deleted in error.
Amended December 7, 1978, effective January 28, 1979. Deletes language pertaining to excess tax reimbursement; amends subsection (b)(1)(E) which provides when leases of tangible personal property are not considered sales; and amends subsection (c)(1) to provide that after 1/1/79 leases of tangible personal property to the United States are subject to sales tax.
Amended March 7, 1979, effective May 16, 1979. Altered definition of “lease”, operative 1/1/79.
Amended February 6, 1980, effective March 29, 1980. Added Sections 6092.1, 6243.1 and 6381.5 to references. In (c)(1) deleted “state and national banks,” and substituted “a federally-chartered bank exempt from direct state taxation under federal law,” and added four conditions for exemption from sales tax; in (c)(8) deleted “bank” and substituted “federally-chartered bank exempt from direct state taxation under federal law.”; in (c)(9)(A) deleted sentences referring to Section 6094(d) and 6244(d); added final paragraph.
Amended August 1, 1980, effective August 22, 1980, operative July 1, 1980. In (b), added (1)(F); in (d), added (8).
Amended November 19, 1980, effective January 16, 1981. In (d)(8)(B) added provisions regarding manufacturer; added paragraph re measure when property not used as residence.
Amended April 1, 1981, effective August 19, 1981. In (b)(1)(E) deleted requirement that lessors prove that retailer paid tax to the Board; substituted “lessor or the transferor has paid sales tax reimbursement.” In (c)(2) added “has paid sales tax reimbursement”; deleted “or their vendor has paid sales tax measured by gross receipts.”
Amended October 26, 1983, effective November 17, 1983. Added last sentence to subparagraph (b)(1)(A) and new subparagraph (2) to subdivision (d), and renumbered former subparagraphs (2) through (8) to (3) through (9).
Amended May 9, 1985, effective September 22, 1985. In Subdivision (c)(1), deleted references indicating that sales tax applies to leases to the United States and its tax-exempt instrumentalities. In subdivision (c)(1), added definitions of “rentals subject

to tax” and provided for the exclusion of certain other charges by the lessor which are not part of rentals. In subdivision (c)(8), deleted references to the United States and its tax-exempt instrumentalities and added reference to the lessee who is “not subject to use tax”.

Amended May 10, 1989, effective July 26, 1989. Amended to include changes necessitated by AB 4417, Chapter 825, Statutes of 1986, and by the holding in *Cedars-Sinai Medical Center v. State Board of Equalization*, 162 Cal.App.3d 1182 (1984). See subdivisions (a)(2)(B) and (a)(3)(A), (B) and (C). Also amended subdivisions (d)(1), (d)(3) and (e) to delete unnecessary language and subdivision (d)(8) to correct a typographical error.

Amended June 5, 1991, effective August 22, 1991. Deleted explanation of the application of tax to leases of certain structures which were entered into prior to 1971. Amended paragraph (b)(1)(F) to limit definition of “mobilehome” for purposes of this regulation to paragraph (a) of Section 18008 and to paragraph 18211, Health and Safety Code. Amended paragraph (d)(8) to delete outdated information and to clarify treatment of leases of factory-built school buildings.

Amended August 1, 1991, effective August 27, 1991. Amended pursuant to Chapter 85, Statutes of 1991, and Chapter 88, Statutes of 1991, to repeal an exemption from sales and use tax for tax on the sale or use of a photograph when possession but not title of the photograph is transferred for the purpose of being reproduced one time only in a newspaper regularly issued at average intervals not exceeding three months. Subparagraphs of paragraph (d) were renumbered.

Amended May 3, 1994, effective July 30, 1994. Added subdivision (a)(3)(D) to define acquisition sale and leaseback, the period of time the provision will be used, and interprets its application to various post-lease transactions.

Amended June 22, 1995, effective July 22, 1995. Deleted subparagraph (a)(3)(D)4. as provided in Statutes of 1994, Chapter 286.

Amended November 5, 1997, effective December 5, 1997. Added new subdivision (b)(1)(F) to incorporate provisions of Chapter 954, Statutes of 1996, and renumbered the following subdivision.